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International Economic & Energy Weekly

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International Economic & Energy Weekly [redacted]

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8 November 1985

Comments and queries regarding this publication are welcome. They may be directed to [redacted] *Directorate of Intelligence,* [redacted]

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International
Economic & Energy Weekly [redacted] 25X1

Synopsis

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1 **Perspective—South Africa: Political Leverage From Regional Trade** [redacted] 25X1

South Africa's dominant influence over the economies of its neighbors limits, in certain respects, Western flexibility in dealing with Pretoria. Effective economic sanctions almost certainly would damage these already weak economies and increase their need for Western economic assistance. [redacted] 25X1

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3 **Sub-Saharan African Trade: Frustration and Failure** [redacted] 25X1

Numerous attempts to increase regional trade and cooperation among Sub-Saharan African countries have had little impact to date, and this situation is not likely to change soon. In our judgment, the lack of trade integration has hindered economic growth as well as efforts to develop closer political linkages. [redacted] 25X1 25X6

[redacted]

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11 **The Airbus Consortium: Growing Product Line Spurs Sales** [redacted] 25X1

Airbus Industrie, Western Europe's four-nation consortium, is having a strong sales year as a result of an expanding product line incorporating advanced aerospace technologies, a new, more international management team, and innovative marketing techniques such as discounts and low interest rates. Over the next few years, Airbus is likely to gain 40 percent of the world large jet aircraft market by 2000. [redacted] 25X1

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15 **Grenada: Struggling To Steer a New Economic Course** [redacted] 25X1

Two years after the US-led military intervention, Grenada is grappling with a 35 to 40 percent unemployment rate as the Blaize administration attempts to reorient the economy toward the private sector. The disappointing pace of new foreign investment and lengthy process of infrastructural development point to slow progress in reducing unemployment. [redacted] 25X1

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Perspective

South Africa: Political Leverage from Regional Trade

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South Africa's dominant influence over the economies of its neighbors limits, in certain respects, Western flexibility in dealing with Pretoria. Effective economic sanctions almost certainly would send shockwaves through neighboring black states. In particular, we believe South Africa would make good its threats to conserve resources in the face of effective sanctions by reducing the flow of oil and other goods to its neighbors. Such retaliation would further damage these already weak economies and increase their need for Western economic assistance. 25X1

South Africa dominates a regional network of economic ties that provides Pretoria with significant economic leverage over its Southern African neighbors. Six of the 10 countries [1] in the region are landlocked and depend on the regional rail network—75 percent of which is under South African control—to reach overseas markets. Alternative rail lines running through Tanzania and Mozambique are unreliable because of insurgent operations and poor maintenance, and ports in these countries are already used to capacity, ensuring that South Africa's transport system handles a large proportion of foreign trade for all six countries. 25X1

Beyond the transport links, the smaller southern African countries import substantial amounts of South African chemicals, machinery, manufactures, grain, and other foodstuffs. While we believe these countries would have little difficulty finding alternative sources should South Africa cut off exports, transportation problems and higher import costs would compound their existing foreign currency shortages and limit supplies of food and manufactures. 25X1

We believe South Africa will continue to enjoy a considerable degree of economic leverage in the region. The smaller southern African countries are likely to remain strongly dependent on South Africa in the areas of trade and transportation, given the vast difference in size and level of economic development between the South African economy and those of neighboring countries, and the failure of institutional efforts, such as the Southern African Development Coordination Conference, to reduce dependence on South Africa. Lack of funds for construction and maintenance of alternative rail and water lines will ensure that South Africa maintains its stranglehold on regional transport. 25X1

[1] Angola, Botswana, Lesotho, Malawi, Mozambique, Swaziland, Tanzania, Zaire, Zambia, and Zimbabwe. 25X1

Pretoria, for its part, almost certainly is wary of establishing even more extensive economic ties that might increase its neighbors' potential counterleverage. South Africa's neighbors publicly have justified their economic relations with the country on the grounds of necessity and have attempted unsuccessfully to reduce their dependence. Despite the benefits generated by these trade links, political tensions and growing mutual distrust are likely to prevent a major expansion of economic relations. 25X1

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Sub-Saharan African Trade: Frustration and Failure

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Numerous attempts to increase intraregional trade and cooperation among Sub-Saharan African countries have had little impact to date, and this situation is not likely to change soon. Regional trade has actually declined over the past 15 years in relative terms and what little intra-African trade exists is dominated by five of the more-developed countries—Ivory Coast, Kenya, Nigeria, Senegal, and South Africa. In our judgment, the lack of trade integration has hindered economic growth as well as efforts to develop closer political linkages.

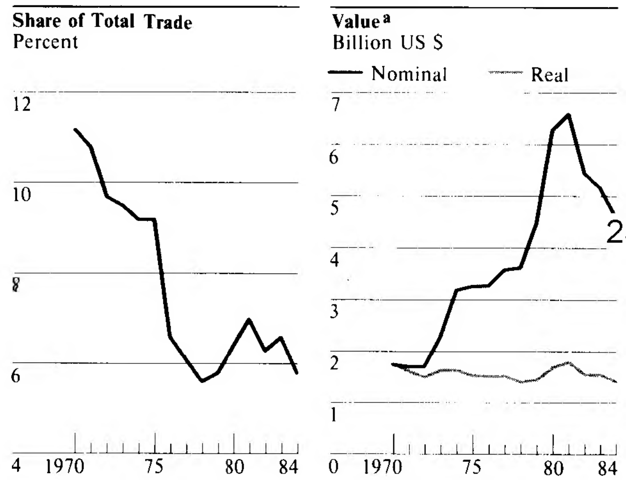
Trade Linkages—Small and Declining

Regional trade, as a percentage of total trade for the Sub-Saharan African countries, has declined over the past 15 years. Last year regional trade accounted for just under 6 percent of total trade, compared to 7 percent in 1981 and over 11 percent in 1970. Several larger countries, including South Africa and Kenya, have seen the percentage decline over the past decade. Others, such as Ivory Coast, Nigeria, and Senegal, have seen little change in the percentage of regional trade. For the smaller African countries as a group, the trade share also has fallen over the past decade.

Since 1981 intraregional trade has been declining absolutely as well as relatively, reflecting the financial difficulties and resulting economic austerity experienced by many Sub-Saharan African countries. In real (inflation-adjusted) terms, regional trade fell 21 percent between 1981 and 1984, dropping below levels achieved during the mid-1970s. Measured in dollars trade fell from $6.6 billion in 1981 to an estimated $4.6 billion last year although much of this was due to the appreciation of the dollar.

The more developed African countries generally suffered the sharpest intraregional trade declines. In dollar terms, South African regional trade dropped by 45 percent between 1980 and 1984, largely due to a sharp fall in regional exports. Cameroon also suffered a loss of 45 percent, while Nigerian regional trade declined by 40 percent.

Intra Sub-Saharan African Trade, 1970-84



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[a] Total trade between Sub-Saharan African countries (exports and imports).

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Intraregional trade, moreover, is dominated by five countries—Ivory Coast, Kenya, Nigeria, Senegal, and South Africa—which accounted for over 50 percent of the total in 1984. This percentage is only slightly lower than in 1974, and is actually higher than the 1970 figure. South Africa alone accounts for more than 20 percent of total Sub-Saharan regional trade, although its importance has slipped in recent years due to the slowdown in economic

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Sub-Saharan African Trade: Top Five Countries Dominate

Million US $

	1970	1974	1980	1984 [a]
Total Sub-Saharan trade	15,642	34,674	98,471	78,920
Total Intra Sub-Sahara	1,746	3,200	6,329	4,590
Top Five	**823**	**1,831**	**3,606**	**2,338**
Ivory Coast	46	183	473	427
Kenya	171	256	439	330
Nigeria	23	207	710	418
Senegal	12	127	182	195
South Africa	571	1,058	1,802	968
Top Five as a share of total intra-Sub-Sahara *(percent)*	47	57	57	51

[a] Estimated.

activity in major regional trading partners such as Zimbabwe and Zambia. The five countries particularly dominate intraregional exports, accounting for two-thirds of the total. They all have relatively well-developed industrial sectors and export considerable manufactured goods to the less-developed African countries, but import little in return.

Sources of Failure

Efforts to boost intra-African trade have centered on formal regional cooperation schemes. Most of these attempts, however, have failed. The most important reason for these failures has been the wide disparity in the level of development and industrialization that has led to domination of trade by a few of the more-developed members. As a result, the poorer countries have tended to leave the group after a short time.

Other factors also have contributed to the lack of regional trade growth:

- Most African leaders see regional cooperation as a way to boost exports rather than imports. The result has been economic policies—such as overvalued exchange rates, high tariffs, and high subsidies—that protect inefficient domestic industries and discourage trade growth.

- Lack of transport, communications, and financial infrastructure has hindered the movement of goods between countries.

- The lack of export diversity among Sub-Saharan African countries.

- Differences in political orientation and mistrust among the countries involved in a regional unit have limited trade expansion. 25X1

Implications and Outlook

The failure to develop intraregional trade has hindered economic development for most Sub-Saharan African countries who are constrained by the small size of their domestic markets. For the poorer, landlocked countries in the region, the lack of regional trade has been especially harmful. In the absence of regional trade linkages, many countries have also wasted scarce resources on a similar range of industries (largely import-substituting), while neglecting agriculture and export-oriented industries. Finally, in our judgment, the absence of strong trade ties has hindered the development of political linkages between African countries, increasing the degree of rivalry and mistrust among nations in the region. 25X1

We believe that there is little hope for any significant increase in the level of intra-African trade in the medium term, given the towering political and economic obstacles to trade expansion. Economic austerity almost certainly will continue in the medium term, holding down import growth. Problems with the lack of export diversity and poor internal transport systems will persist, as financial 25X1

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Intra Sub-Saharan African Trade as a Share of Total Sub-Saharan Trade

Percent

	1970	1974	1980	1984 [a]
South Africa				
Exports	11	8	6	4
Imports	5	5	2	2
Senegal				
Exports	3	20	30	26
Imports	4	10	4	5
Ivory Coast				
Exports	5	12	12	11
Imports	6	4	4	4
Nigeria				
Exports	1	2	2	2
Imports	1	1	1	2
Kenya				
Exports	40	34	26	23
Imports	11	5	3	1
Cameroon				
Exports	7	8	7	5
Imports	9	9	10	4
Gabon				
Exports	7	4	3	2
Imports	2	7	5	5
Malawi				
Exports	12	18	15	17
Imports	26	19	44	28
Liberia				
Exports	1	1	2	1
Imports	1	3	2	1
Zambia				
Exports	1	2	5	5
Imports	14	12	4	9
Zaire				
Exports	24	2	1	1
Imports	8	7	4	4
Tanzania				
Exports	17	18	14	7
Imports	15	8	3	11
Mozambique				
Exports	10	10	12	14
Imports	3	3	4	8
Somalia				
Exports	3	5	2	1
Imports	9	12	11	4
Zimbabwe				
Exports	NA	NA	13	18
Imports	NA	NA	22	14

[a] Estimated.

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difficulties leave little funding available for development projects. The larger, more-developed African countries, such as South Africa, Ivory Coast, and Nigeria also are likely to continue to account for most regional trade.

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Efforts at Regional Integration

The South African Customs Union (SACU)*—made up of Botswana, Lesotho, South Africa, and Swaziland—has been in existence for nearly 75 years. The gains in regional trade stem largely from the geographic dependence of the smaller members on South African transport links. The customs union has strengthened trade ties among these countries, with the smaller members substituting South African imports—such as foodstuffs and capital goods—for imports originating outside SACU.*

The West African Economic Community (CEAO)*—Benin, Burkina, Ivory Coast, Mali, Mauritania, Niger, and Senegal—has achieved a marked increase in regional trade, in part because some non-CEAO imports have been replaced with imports from the community. In contrast to other regional groupings, poorer countries such as Burkina, Mauritania, and Mali have shown strong gains in regional exports.*

The East African Common Market*—made up of Kenya, Uganda, and Tanzania—was set up in 1967 to promote trade and cooperation among these former British colonies. During its 10 years of existence, regional trade declined as a percentage of total trade.*

The Economic Community of West African States (ECOWAS)*, an ambitious attempt at regional integration, includes some of the poorest countries of the Sahel region and relatively developed nations, such as Nigeria and Ivory Coast. Intraregional trade has not increased since the formation of ECOWAS in the mid-1970s, and accounts for only 3 percent of total trade of the countries in the group.* 25X1

The South African Development Coordination Conference (SADCC) *was formed in 1980 as an attempt by black Southern African countries (Angola, Botswana, Lesotho, Malawi, Mozambique, Swaziland, Tanzania, Zambia, and Zimbabwe) to forge regional trade ties and reduce economic dependence on South Africa. Intra-SADCC trade accounts for only 4 to 8 percent of total SADCC trade, and all member countries still have close trade ties to South Africa.* 25X1 25X1

The Customs and Economic Union of Central Africa (UDEAC)*—consisting of Cameroon, Congo, Gabon, Equatorial Guinea, and the Central African Republic—is an effort to promote trade among Equatorial African states. Intra-UDEAC trade has not increased substantially, and, if Cameroon is excluded, intraregional trade has actually fallen.* 25X1 25X1

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The Airbus Consortium: Growing Product Line Spurs Sales [redacted]

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Airbus Industrie, Western Europe's four-nation consortium, is having a strong sales year as a result of an expanding product line, advanced aerospace technologies, a new, more international management team, and innovative marketing techniques such as discounts and low interest rates. For the first nine months of this year, Airbus has captured slightly over 35 percent of the unit sales in the large jet commercial market, including over 50 percent of the widebody market and several large orders for its all-new, 150-seat, narrowbody A320. We believe a growing product line, combined with a major marketing campaign, will bring additional sales success over the next few years, and Airbus is likely to gain 40 percent of the world large jet aircraft market by 2000. [redacted]

Growing Order Book

After a slow start in the 1970s, the French-led Airbus consortium now has firm orders for some 500 aircraft from 57 airlines. Airbus captured over one-third of the widebody market between 1979-85 and is achieving good success with the all-new, 150-seat A320 design scheduled to enter service in 1988. Sales to date for the narrowbody A320 total 109, with options for 125 more. [redacted]

This year alone Airbus has sold 92 aircraft valued at some $3.2 billion—58 A320s and 34 widebody A300s and A310s—compared with total sales of 35 aircraft in 1984. More important is the growing list of first-time customers. The sale to Pan Am, which industry experts call the "deal of the century," involved a firm order for $1.1 billion in aircraft and included the first US purchase of the A320. More recently, Lufthansa, traditionally a US buyer, purchased up to 50 aircraft valued at $2 billion. [redacted]

With the big inflow of new orders, industry experts expect Airbus to increase production from the present three per month to at least four per month, starting in early 1986. Moreover, we believe existing tooling, jigs, and available workforce at all sites would permit a further increase in production in 1987 if sales warrant. [redacted] 25X1

Airbus Advanced Technology

Many Western aerospace experts believe a key ingredient in Airbus sales success has been the consortium's willingness to apply advanced technologies to new aircraft designs. We believe Airbus 25X1 Industrie intends not only to meet US competition, but also surpass it by building aircraft containing the latest engineering know-how. To accomplish this goal, the consortium is investing heavily in advanced cockpit technologies for the A320 and research and development work for the entire product line in advanced materials such as composites and aluminum-lithium alloys, and computer-aided design (CAD). [redacted] 25X1

The Airbus R&D efforts are already paying dividends. The derivative A310-300 design has an all-composite fin that gives a 20-percent weight savings over the conventional aluminum fin and is the first airliner to enter series production with a major composite element. We estimate Airbus' use of such composites will give Europe a three- to five-year lead over the United States in commercial applications of composite materials to large passenger jets. [redacted] 25X1

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Airbus engineers are presently setting up a trans-European CAD system that links the four members

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of the consortium. Aerospatiale has developed a software system that allows transmission of drawings and machine tool programing information among the companies. In the past, incompatible CAD systems made this integrated design effort impossible. The new system eliminates the exchange of microfilmed drawings and, in some cases, the transfer of actual full-scale models of parts.

The "Family" of Aircraft

The A320's success has laid the groundwork for the next phase in the development of the Airbus "family" of aircraft. The two new designs most talked about are the very long-range, medium capacity, four-engined TA11 and the long-range, large capacity, twin-engined TA9. Airbus is also planning additional versions of the A320. The TA11 would carry about 250 passengers some 6,000 miles (nearly 10,000 kilometers) and is targeted at replacing aging DC8s and 707s. This design is strongly backed by Lufthansa. The TA11 has been referred to as the A330 by some Airbus officials, a signal they may be close to a program start. Airbus' President Pierson has stated the order base would need to be similar to that of the A320, approximately 50 to 60 aircraft from three to four airlines.

The TA9, a stretched version of the A310, would carry about 330 passengers over distances of about 4,000 miles (roughly 6,000 kilometers). It would also effectively replace many existing trijets like the Lockheed Tristars and McDonnell Douglas DC10s on short- to medium-range routes, and introduce twin-engine economy to this sector of the market. The TA9 is a logical extension of the Airbus product line. Although no airline has stepped forward, we believe a market exists in the late 1990s for a plane to satisfy the routes that do not require the seating capacity of the 747. Airlines in South Asia, the Far East, and Latin America are potential customers.

A320: Advanced Technologies in the Cockpit

An important ingredient in the recent sales success of the A320 has been the advances in automated cockpit technology. These improvements facilitate aircraft operation, save weight, and reduce maintenance costs. The A320 will be the first airliner to be equipped with the following innovations: 25X1

- *Digital flight controls combined with side-stick controllers. The digital flight controls is an electrically signaled system, also known as fly-by-wire. The concept is based on two independent computer systems and simplifies aircraft operation. The use of side-stick controllers allows elimination of the traditional yoke and gives the pilot an unobstructed view of the instrument panel.*

- *Integrated flight-control and flight-management systems. The result is the Flight Management Guidance Computer, which makes possible the elimination of several avionics systems. The guidance computer continuously supplies command signals through the fly-by-wire computers to handle most of the actual flying of the aircraft.*

- *Color cathode ray tubes (CRT) in place of electro-mechanical instruments. The CRTs provide a clear, uncluttered presentation of data.* 25X1 25X1

International Approach to Management

A good part of the sales success stems from a more aggressive management team—once dominated almost exclusively by the French—which came into office early this year. The new Franco-German leadership has created several new management divisions in an effort to increase efficiency and to

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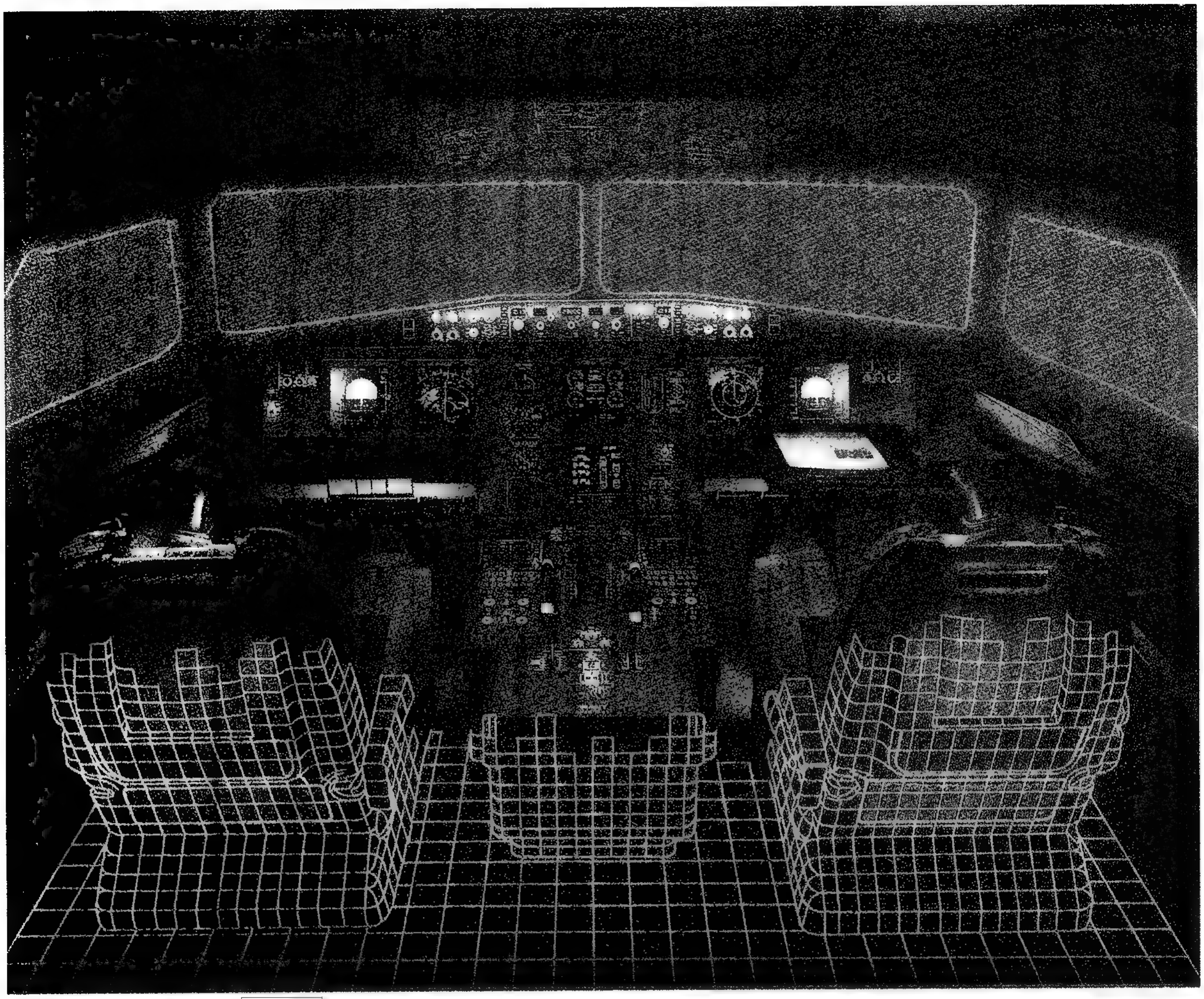

A320 Automated Cockpit. [redacted]

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improve financial accountability to its partners. Pierson has stated that Airbus is planning more aggressive marketing of aircraft in the United States, including the sale of secondhand airplanes taken in trade to the small airlines in the United States. With a British national leading a division wholly responsible for all financial matters, London—notoriously slow in appropriating money for new projects—will have a direct voice in Airbus's affairs. [redacted]

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Aggressive Marketing

The sales success of the Airbus also is closely tied to aggressive marketing techniques, innovative financing, and government support. Many Western aerospace experts report that present aircraft deals are increasingly being determined on financing rather than on product comparisons. [redacted]

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The recent Pan Am purchase is an example of innovative arrangements. Because of Pan Am's financial problem, the deal was structured as a lease instead of an outright sale. Pan Am will pay for the aircraft over a predetermined period of time and then return them for newer planes and all-new financing. As a result, Airbus was able to cut its inventory of unsold aircraft and will sell the returned airplanes on the used market. [redacted]

Similar innovative moves were taken when Lufthansa in mid-1985 was balking at purchasing the A320. [redacted] The conditions included a right to cancel for any reason until mid-1988 and to cancel within two years after the delivery of the first A320 if a superior alternative such as the Boeing propfan becomes available. [redacted]

Direct French Government support apparently was a key factor in the recent sale to Indian Airlines. [redacted]

Outlook

We believe that Airbus probably will gain 40 percent of the world large jet aircraft market by 2000. Airbus Industrie's growing sales success, coupled with plans for further expansion of the consortium's product line, will make it more difficult for new US programs to be profitable. Indeed, the A320 is having success in the 150-seat category that will not have an all-new US competitor until 1992-95. [redacted]

For the longer term, we believe the current marketing success will accelerate Airbus plans to expand its product line—most likely the TA11—and become more competitive across the board with US manufacturers. The A320 itself is likely to evolve into a series of derivatives with various capacities and ranges. A wider selection of aircraft will further enhance Airbus's image with airlines around the world. [redacted]

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Grenada: Struggling to Steer a New Economic Course

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Two years after the US-led military intervention, Grenada is grappling with a 35- to 40-percent unemployment rate as the Blaize administration attempts to reorient the economy toward the private sector. The government's effort to stimulate development of agriculture, tourism, and light manufacturing is hampered by the island's weak infrastructure, which has discouraged any significant inflow of foreign investment. Sizable aid from Western donors, particularly the United States, probably will enable Grenada to achieve moderate economic growth over the near term. Still, the disappointing pace of new foreign investment and the lengthy process of infrastructural development point to slow progress in reducing unemployment. If hopes for continued economic improvement fade, discredited political elements—both the right and the radical left—could capitalize on the public's disillusionment.

Restructuring After the Bishop Years

During its four years in power, the People's Revolutionary Government of Maurice Bishop implemented economic and political policies that weakened the Grenadian economy—real GDP grew at an average annual rate of only 1.8 percent in 1979-83, compared to a yearly average of 7 percent during 1975-78. Despite expansion of the army and featherbedding in the public sector, unemployment was estimated to have been as high as 27 percent during the early 1980s. Moreover, the population—officially listed in the 111,000 to 118,000 range—may well have fallen to 85,000 as many skilled Grenadians fled the adverse economic and political environment.

Following the US-led intervention in October 1983, the interim government began to reorient Grenada's economy toward the private sector. It revised the country's investment code to open virtually all sectors to private investors and introduced investment incentives comparable to those of other Caribbean countries. In addition, by late 1984, the government had:

- Relinquished control of the nutmeg, banana, and cocoa associations and returned a number of agricultural estates to private hands.
- Laid off hundreds of state employees.
- Lowered the stamp duty on imports by 25 percent in an attempt to ease the island's cost of living, stimulate consumer demand, and encourage private investment.
- Raised ceilings on interest rates to encourage private saving.
- Relaxed foreign exchange controls in an effort to improve business confidence in the new, free-market economy. 25X1

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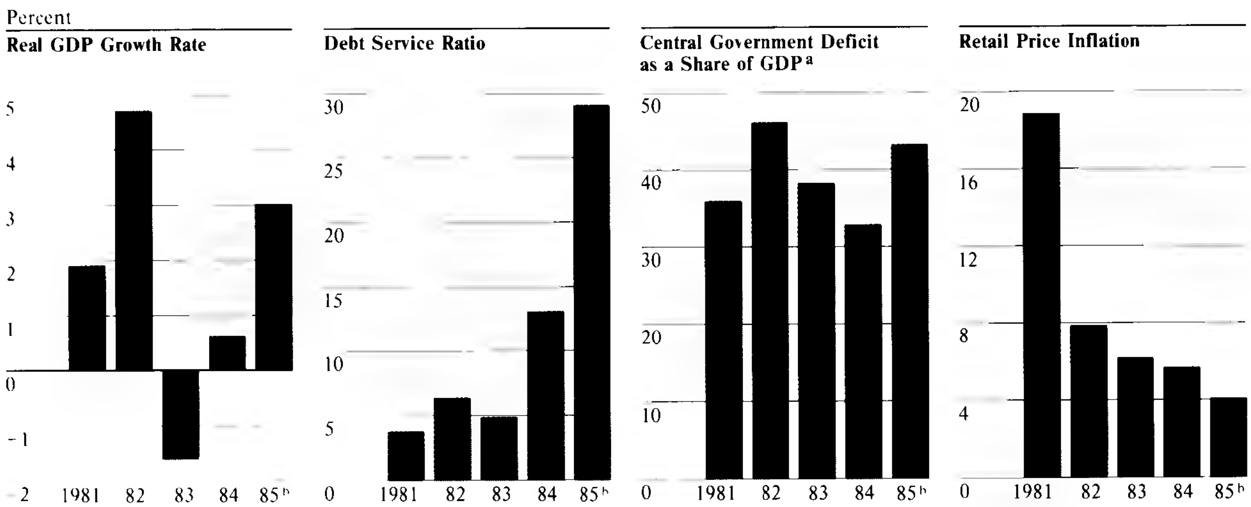
With the end of Soviet Bloc funding—as well as the termination of a three-year, $14 million IMF program arranged just before Bishop's downfall—the interim government looked to Western countries for financial support. According to World Bank and IMF data, a record $25 million in external grants was disbursed to the Grenadian Government during 1984. Aid from the United States—by far the largest donor—and Canada enabled construction of the Point Salines airport to be largely completed by late 1984. 25X1

Challenges Facing the Blaize Government

Despite this promising start, formidable economic problems have persisted since Prime Minister Herbert Blaize was elected in December 1984. Foremost is unemployment—now 35 to 40 percent—concentrated among the country's youth. 25X1

Grenada: Economic Indicators, 1981-85



[a] Excludes external grants.
[b] Projected

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The government is especially worried about joblessness among students who have returned from Cuba and former soldiers of the disbanded People's Revolutionary Army.

To ease unemployment, the Blaize administration is targeting agriculture, tourism, and light manufacturing for rapid development:

- Substantial funds have been directed toward upgrading agricultural productivity and expanding support services. The island's cocoa and banana cooperatives have received funds to cover financial shortfalls due to slumping world prices. The government also is selling farmland on concessional terms to small-scale farmers.

- Tax holidays of up to 10 years are being offered to investors in tourism. The government is scheduled in December to start its own airline—Grenada Airways—to facilitate the flow of tourists to the island. Grenada Airways also plans to eventually build a 300- to 350-room hotel near the Point Salines airport.

- New investment in light manufacturing is also eligible for lengthy tax holidays. In 1985, the corporate income tax was reduced slightly, and an Industrial Development Corporation was established to promote and coordinate new investment projects.

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Still, Grenada's weak infrastructure, which the US Embassy compares unfavorably even with Haiti and such ministates as Antigua, St. Kitts, and St. Lucia, seriously restrains the inflow of investment needed to spur growth in these sectors. Electric power is inadequate even for current needs, and frequent blackouts interrupt other services, such as telex and telephone communications as well as the provision of water and cooking gas. The telephone system also is severely strained; there are more than 2,700 service applications on a growing waiting list and only 15 long-distance lines to the island. The development of tourism on the southwest coast

Grenada: Western Economic Aid Commitments, 1984-85 [a]

Million US $

	1984	1985
Total	**46.5**	**55.8**
Loans	4.8	7.2
Caribbean Development Bank	2.7	2.9
United Kingdom	1.5	2.6
Other	0.6	1.7
Grants	41.7	48.5
Canada	7.5	5.0
Airport construction	6.1	3.3
European Development Fund	0.7	1.4
United Kingdom	1.4	0.4
United States	30.7	27.2
Airport construction	18.0	12.1
Other and unspecified	1.4	14.5

[a] Based on Grenadian Government estimates.

[redacted]

is hampered by insufficient water distribution and sewage disposal. In addition, the number of rooms available to accommodate tourists has dropped to 397. Meanwhile, years of neglect have caused serious deterioration of the island's road network. Agriculture, which employs one-third of the work force and is Grenada's largest foreign exchange earner, suffers substantial losses of perishable produce because of the poor condition of farm roads. [redacted]

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Other disincentives to foreign private investment include memories of the island's political instability and long bureaucratic delays in approving investment proposals. Moreover, Grenada's inadequately trained work force has partly offset the comparative advantage of relatively low-cost labor. [redacted]

To cope with severe cash-flow problems, the Blaize administration resorted to heavy domestic borrowing this summer to meet payroll needs. With Grenada's external debt doubling to more than $50 million since 1980, the country's debt service burden has increased dramatically and further strained public finances. In August, the Cabinet cut operating expenditures by 10 percent in an attempt to trim the fiscal deficit. [redacted]

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Near-Term Prospects

Sizable aid inflows, particularly for the construction sector, probably will allow Grenada to continue moderate growth, but lagging foreign investment and the slow process of infrastructural development suggest that little progress will be made against unemployment over the next year or two. Tourism is likely to receive a boost as Grenada Airways and a large, new, privately-managed hotel begin operations soon. Still, the government will continue to face tight fiscal constraints. Until aid-financed infrastructural projects are in place—probably well into 1987—the island will remain heavily dependent on US and other foreign budgetary support. [redacted]

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Continued high unemployment will increase the potential for popular disillusionment with Grenada's new economic and political course. If hopes for prosperity fade, opposition groups on both the right and the radical left would try to capitalize on growing public discontent. [redacted] 25X1 [redacted] the socialist Maurice Bishop Patriotic Movement already is working to regain social and political acceptance through youth and trade union groups. 25X1 Eric Gairy, the autocratic former Prime Minister toppled by Bishop, tried in September to bolster his political fortunes by leading agricultural workers in a wage strike. Although shortlived and unsuccessful, the strike demonstrated that at least some segments of the population remain susceptible to political manipulation. [redacted] 25X1

[redacted]

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Zambia: Struggling With Austerity

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Declining copper production and falling world copper prices have slashed Zambia's exports by more than one third since 1980, causing goods shortages, inflation, and three consecutive years of economic contraction. President Kaunda—with IMF backing—has imposed a series of tough reforms in an effort to reduce consumer demand for imports and reverse balance-of-payments deficits. Currency devaluations totaling almost 90 percent since 1980 have been the centerpiece of the reform program. Although opposition to this belt-tightening has been muted so far, massive foreign debt problems will enforce continued austerity through 1986 and beyond, resulting in rising political pressures on Kaunda's long-dominant position.

Copper Drags Down the Economy

The Zambian copper industry, which provides 90 percent of the country's exports, is suffering from a variety of domestic and international problems. Costs are high because of the depletion of some of the richer and more accessible ore deposits and because of gross overstaffing—output per worker is barely one-tenth the US level. Based on incomplete data published by the US Bureau of Mines, we estimate that average production costs at Zambian copper mines are currently about $1 per pound of copper—about 50 percent above the current world copper price. In addition, the government has sought to conserve foreign exchange in the short run by cutting foreign exchange allocations to the mining sector. This has caused shortages of fuel and other supplies while forcing mines to continue operating aged equipment at reduced rates of utilization and to cannibalize machinery for spare parts.

On the international level several factors have caused world copper prices to drop by about one-third since 1980. Industrial demand for copper continues to decline, and major low-cost producers such as Chile are increasing output and exports. As a result, even the strong economic growth since 1982 in the United States and other developed markets has not resulted in an upsurge in copper prices. 25X1

Copper production in Zambia has fallen from 610,000 metric tons in 1980 to about 500,000 tons this year, according to our estimates. Coupled with the fall in international copper prices, this has cut the value of total Zambian exports by more than one-third since 1980 to about $900 million this year, with disastrous consequences for the economy: 25X1

- Real GDP has been zero or has contracted in every year since 1981.
- Foreign debt has doubled since 1980, and the debt service ratio has risen to an unmanageable 70 percent in 1985, despite three debt rescheduling agreements in 1983 and 1984.
- Imports have been cut by 50 percent, causing severe shortages of consumer goods, fuel, and raw materials.
- Manufacturing and processing industries are operating at only about 30 percent of capacity, according to estimates quoted by President Kaunda in a recent speech.
- Inflation has risen steadily to about 20 percent in 1985. 25X1

Reform Efforts

Lusaka has taken major strides in cooperation with the IMF to adjust to the decline in foreign exchange earnings. The effort has included successive currency devaluations, cuts in government spending, higher producer prices to boost output of 12 major farm commodities , and elimination of controls on the prices of cornmeal and many consumer goods. In January of this year, however, following 25X1

Zambia: Current Account, 1980-85 *Million US $*

	1980	1981	1982	1983	1984	1985 [a]
Current account	**−627**	**−826**	**−616**	**−169**	**−115**	**0**
Merchandise trade balance	343	−69	−56	271	304	400
Exports	1,457	996	948	982	916	900
Imports	1,114	1,065	1,004	711	612	500
Net services	−970	−757	−560	−440	−419	−400

[a] Estimated.

[redacted] 25X1

two successive standby agreements totaling nearly $460 million, the IMF ended disbursements of standby funds because of Zambia's inability to meet interest payments on debt owed to the IMF and its refusal to follow IMF recommendations for a devaluation of more than 50 percent. This fall, the continued decline in copper production and the intractable growth of debt service obligations induced Kaunda to push through two key new IMF-recommended reform measures: a sharp reduction of corn subsidies in September and a weekly foreign exchange auction system in October. The auction, which now has functioned for five weeks, has resulted in a two-thirds devaluation of Zambia's currency since September. These measures have brought about dramatic price increases—40 percent for cornmeal and over 100 percent for major imported commodities, such as petroleum products. [redacted]

Popular reaction to Kaunda's tough economic reform program so far has been limited largely to short-lived strikes, such as those by mineworkers in mid-1985 and by Lusaka's taxi drivers in October. More ominously, the Zambian Congress of Trade Unions—which includes all 18 of Zambia's labor unions—plans to ask the government for a 100-percent pay hike and to threaten a general strike if turned down. The general public, including the lower ranks of the military and the nation's farmers—upset over a profit squeeze—have confined themselves to grumbling. The generally muted response in light of practically universal opposition to the austerity measures partially reflects the care taken by Kaunda to provide offsetting economic perks to key groups, such as significant military pay increases in October just prior to the introduction of the foreign exchange auction. Wage and salary increases also were announced for civil servants and are planned for unionized industries, according to Embassy reporting. [redacted] 25X1

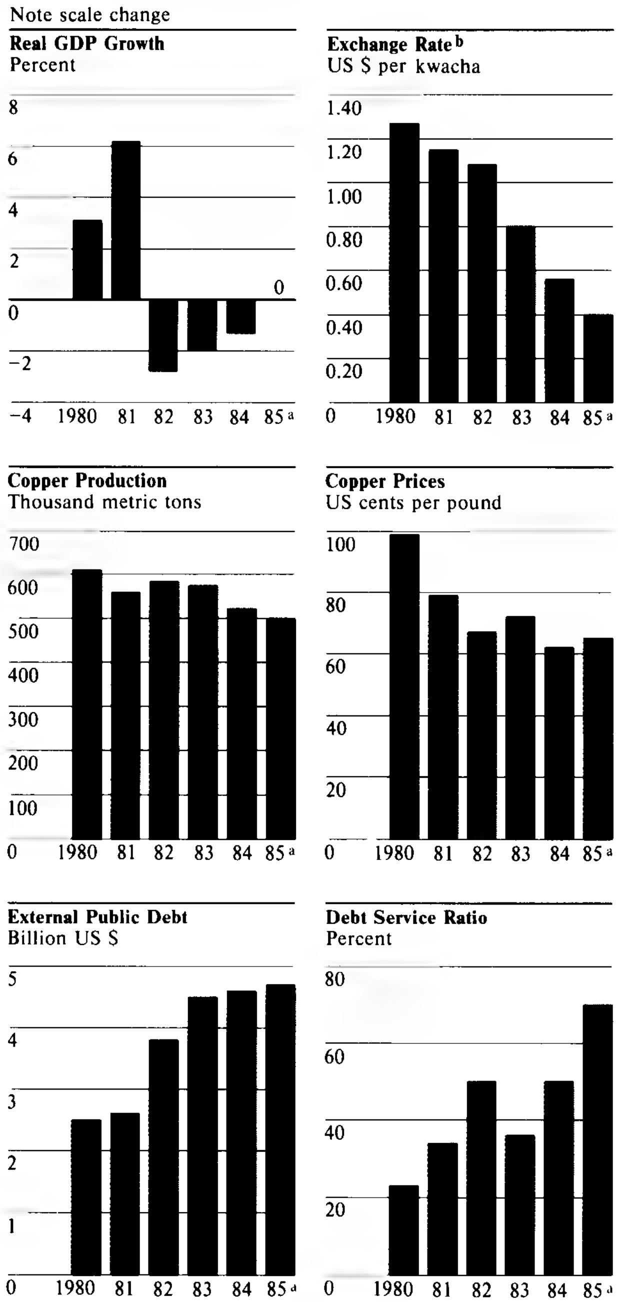
Economic Outlook

Although no increase in real GDP is likely this year or next, the three-year slide in output appears to have ended, at least temporarily: 25X1

- A return to normal weather this year after two years of drought has resulted in a sharp improvement in farm production. 25X1

- The completion of a $300 million mine rehabilitation program in 1986 will bring a temporary end to the decline in copper production although no significant increase in foreign exchange earnings is expected. [redacted] 25X1

Zambia: Economic Indicators, 1980-85



[a] Estimated.
[b] Average exchange rate for each period.

307381 11-85

In our view, prospects are dim for developing major sources of foreign exchange outside the copper industry. Government policies—including price incentives and efforts to streamline the cumbersome, government-run marketing system—so far have focused on efforts to stimulate agriculture both to produce commodities for export and to reduce requirements for imports of raw materials for food-processing factories. Despite its considerable potential, however, agriculture will not easily offset the employment and foreign exchange losses from the copper decline even under the best of circumstances because of the country's limited cultivable acreage and the likely reluctance of mine and industrial workers to transfer to farm jobs. 25X1

Deep cuts in imports because of devaluation and reduced imports of farm commodities, plus the prospective leveling off in copper production, will produce a small current account surplus next year for the first time since 1979, according to our estimates. Zambia's foreign debt, however, now totals about $4.7 billion, according to press reports, almost double the country's GDP. Even limited attempts by Lusaka to service the massive foreign debt would virtually wipe out any economic relief from the prospective current account surplus. Likely attempts by Lusaka to catch up at least partially with overdue payments just to the IMF would require up to 40 percent of export receipts, according to press reports. 25X1

Toughing it Out

Despite dismal prospects for the economy, Kaunda appears to be firmly committed to economic reform, and, in the short run, a number of factors may run in his favor. His efforts to alleviate the impact of economic austerity on key groups such as the military appear to be working, at least for now. The leadership of major nonunion institutions such as the military, is closely allied with Kaunda's political party, and we believe that Kaunda can continue to count on at least grudging acquiescence by most major public figures in his efforts to achieve economic reform.

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Kaunda, moreover, may be able to capitalize politically on the short-run economic impact of better crops and the temporary end to the decline in copper production in 1986, despite the lack of any significant benefit to hard-hit Zambian consumers. Further large auction-related currency devaluations anytime soon are unlikely, according to Embassy reporting. The introduction of the foreign exchange auction, moreover, and possible efforts to reduce overdue interest payments to the IMF may pave the way for another IMF standby agreement. [redacted] 25X1

Kaunda, nonetheless, is bound to lose some popular support over the longer term as austerity drags on and economic recovery proves elusive. Per capita GDP already has fallen by more than one-fifth since 1980, and we believe prospects for wildcat strikes, consumer riots, or other spontaneous outbreaks of violence will increase as living standards continue to erode. The potential for organized opposition is greatest from Zambia's powerful labor unions, whose membership numbers over 200,000 and includes most workers in mining, industry, and construction. The country's history of labor turbulence and growing rank-and-file pressures on labor leaders for wage adjustments almost certainly will lead to more serious strikes or work stoppages. [redacted] 25X1 Although we expect the military to continue to back the regime, this support could erode if Kaunda is forced repeatedly to call on troops to help put down civil disturbances. Political pressures will be increased by likely recurrent shortages of foreign credit needed for imports of petroleum products and other critical commodities because of the size of the overdue debt and debt servicing requirements. [redacted] 25X1

[redacted] 25X1

Briefs

Energy

OPEC Oil Pricing Policy in Disarray

[redacted]

Recent statements by OPEC members reflect the growing disarray over pricing policy and indicate the increasing irrelevance of OPEC's official prices. UAE Oil Minister 'Utayba publicly claims that OPEC members will no longer be subject to official price guidelines. Indonesia's Oil Minister, however, denied that the OPEC price structure has been abandoned. Saudi Oil Minister Yamani recently asserted that future oil prices would be determined both by major oil companies and by OPEC. Mexico decided last week to adjust its oil prices to make them more in line with market conditions. Low oil inventories and rising winter consumption appear likely to prevent a major price break before OPEC ministers meet in December. This reprieve probably will be only short lived, however, especially if OPEC members attempt to increase revenue further through additional price cuts. [redacted] 25X1

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[redacted]

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Iran's New Oil Minister Favors Increased Countertrade

[redacted]

[redacted]

Iran's new Oil Minister, Qolam Reza Aqazadeh, told the parliament (Majles) he favors linking purchases of foreign goods to oil sales, according to the Iranian press. Although Aqazadeh also said he wants to maintain OPEC's cohesion, he is closely connected with radicals who favor increasing Iran's oil production—Iran has excess production capacity of about 1 million b/d. His predecessor, Mohammad Qarazi, had been criticized for his inability to maintain oil revenues. A former head of the committee that organizes Iran's oil barter deals, the new oil minister will probably push aggressively for increasing oil sales through countertrade arrangements, but will be reined in by Majles's concern that boosting oil exports sharply could collapse the oil market. [redacted] 25X1

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Canadian Natural Gas Policy

[redacted]

Ottawa's decision last week to partially deregulate the natural gas industry may add to strains among the energy- producing and-consuming regions and impede efforts to promote freer trade with the United States. The new policy is designed to allow Canadian producers to increase their natural gas exports to the United States by basing export floor prices on regional prices rather than a single national price. The major consuming provinces, left out of the final negotiations between Ottawa and the producing provinces, were outraged at the decision to freeze domestic wholesale energy prices at a rate higher than the level likely in a free market. Leaders of consuming provinces fear their industries would lose competitiveness vis-a-vis US firms if US natural gas prices—now higher than Canadian prices—fall below the now-frozen Canadian level. In this event, Ottawa's ability to negotiate a freer-trade pact will be hampered. Ottawa, however, would likely be quick to adjust domestic energy prices if US gas price levels drop sharply. [redacted] 25X1

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Soviet-Japanese Natural Gas Discussions

[redacted]

Soviet Deputy Foreign Trade Minister Sushkov will visit Tokyo this month to try to break the deadlock on terms for jointly developing the 4.3 billion-cubic-meter-per-year gas project on Sakhalin Island. Japanese utilities have not yet committed themselves to buy any gas, nor have the terms of Japanese loans for the project been set. According to the Japanese press, Sushkov is threatening not to place a $3 billion order for a petrochemical plant with Japanese firms unless Tokyo guarantees the amount of its gas purchase and the loan terms. A final decision on the Sakhalin project—which has been under consideration for nearly 20 years—may come as soon as early 1986. Although Japanese gas supplies are set well into the 1990s, the Japanese decision on whether to take some Soviet gas in the late 1990s may be determined as much by a desire to win some project contracts for Japanese firms as by anticipated gas requirements. [redacted] 25X1

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Japan Revises Gasoline Import Plans

[redacted]

Japan will begin to import gasoline sooner than previously expected, but only on a small scale, according to the US Embassy. Embassy reporting indicates the startup date for imports was moved from April to January in response to strong US pressure. MITI will introduce legislation later this month allowing it to control the quantity of gasoline imports despite Tokyo's earlier claims that volumes would be determined only by market forces. MITI faces strong opposition from domestic refiners, and press [redacted] sources believe the Ministry will strongly resist foreign pressure to increase imports beyond 2 million kiloliters in 1986—about 5 percent of Japanese demand and well below the import levels envisioned by US and European policymakers. In addition, Tokyo—ever mindful of the oil shocks of the 1970s—continues to be wary of dependence on foreign refiners. [redacted] 25X1

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USSR Expanding Energy Cooperation With Vietnam

[redacted]

Moscow will quadruple oil exploration and development assistance to Vietnam in the coming five years under the plan for the Soviet-Vietnamese joint venture, Vietsovpetro. The venture is planning to step up operations in the offshore Bach Ho field—where it first discovered oil in 1984, but has not yet completed delineation drilling. Two production platforms are nearing completion and another is being erected. Hanoi hopes to reduce its dependence on the USSR for its oil imports, which amounted to nearly 35,000 b/d in 1984. [redacted] 25X1

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Yugoslav Energy Cuts

[redacted]

Croatia and Slovenia have joined the republics of Bosnia-Hercegovina and Montenegro in announcing energy conservation measures. The new regulations restrict the use of street lighting, forbid neon and other electrical signs, and ban late-night television and the use of supplementary heaters in offices and public areas. A continuing drought has reduced reservoir levels at hydroelectric plants to 20 percent below normal. Power cuts in 1984 curtailed industrial output and visibly soured the public mood. The energy situation is potentially more serious this year, especially in Croatia. Officials there have already expressed concern that imported fuel oil, dependent on limited foreign exchange, may be in short supply this winter. Up to one-third of Croatia's generating capacity relies on fuel oil. Unless rains come soon, these first-phase reductions could escalate into more widespread power cuts this winter. [redacted] 25X1

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International Finance

[redacted]

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New Delay in Philippine IMF Program

[redacted]

Manila's burgeoning budget deficit will delay until December at the earliest the third disbursement of $106 million from the IMF's $615 million balance-of-payments loan. According to US Embassy reporting, unexpectedly low tax receipts and massive subsidies to shaky government financial institutions are pushing this year's budget deficit to over $1 billion—nearly triple the Fund's target. Even if agreement can be reached on the new taxes and expenditure 25X1

cuts required to trim the deficit, disbursements will be delayed if the Fund determines that Manila concealed information on various tax exemptions—as some observers charge. Until the IMF program is back on track, Manila's commercial creditors will postpone new loans—undercutting Manila's efforts to portray uninterrupted progress with the financial rescue package. Although a one month delay will not erode Manila's foreign exchange reserves—now equal to three months of imports—a lengthy interruption in the Fund program would threaten the fragile economic recovery, which seems to be on the horizon. ([redacted] 25X1

Peru's Increasing Financial Isolation

[redacted]

President Garcia's refusal to back away from his hard line on debt is increasingly isolating Peru from international lenders. Meanwhile, Garcia is bracing against reprisals. [redacted] To mitigate the loss of trade credits, Lima has built its foreign exchange reserves to about $2 billion, according to the Central Bank, and has extended the current freeze on dollar accounts for six months. Under Garcia's repayment scheme—limiting debt service to 10 percent of exports—commercial banks will probably receive no debt payments for at least another nine months. He is apparently preparing to use his replenished reserves and trade surplus to purchase essential imports, and he may try to strengthen commercial ties to the Soviets. Garcia will probably increase his rhetoric against "financial imperialism" to retain support at home and to coerce bankers into accepting longer repayment periods, debt service payments in kind, or payments tied to the prices of Peru's exports. Should creditors balk, Garcia might go so far as to repudiate the external debt outright. [redacted] 25X1

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Sudan's Prospects for IMF Agreement Fade

[redacted]

An IMF negotiating team has left Khartoum again with no agreement in sight on Sudan's arrearage problem. According to the US Embassy, the Fund is beginning to doubt that international donors will provide the large cash grants necessary to cover Sudan's IMF arrears, which currently total about $200 million. The United States and Saudi Arabia together have pledged $70 million toward meeting IMF arrearages, but other donors remain noncommittal. Following a recent conference in Riyadh, Kuwait, Saudi Arabia, and the UAE agreed to extend bridge loans to cover $145 million in Sudanese arrears to the Arab Fund but did not provide any additional financial assistance. The IMF reportedly sees little value in reaching agreement on a reform package without resolution of the arrearages and may, in a last minute move designed to loosen up donors, threaten to declare Sudan ineligible for further IMF financing. [redacted] 25X1

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Global and Regional Developments

London Warming Up to EUREKA

[redacted]

London apparently is showing more interest in EUREKA, France's proposal for European cooperation in high technology, hoping to reap economic and political benefits and remind Washington that alternatives exist to SDI research. According to the financial press, the Department of Trade and 25X1

Industry is seeking Treasury approval for a special contingency fund to help finance EUREKA-related research, as well as to better coordinate spending on civilian R&D. Until now, the government was planning to fund EUREKA out of existing technology support programs. London remains adamant, however, that the primary initiative for EUREKA participation come from private industry. Greater support for EUREKA reflects the Thatcher government's general concern over insufficient private investment in civilian R&D programs. While the government probably plans to spend only a marginal sum to spur technological development, it wants to take credit for any business profits or new jobs that result if EUREKA takes off. In any case, this attention to EUREKA would increase London's options for greater cooperation with the EC should US funding of SDI research not meet British expectations. [redacted]

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Problems For European Semiconductor Project

[redacted]

Megaproject—the joint program between Siemens of West Germany and Philips of the Netherlands to develop advanced random-access memory chips—almost certainly will be hampered by Siemens' inability to take full advantage of its recent cooperative agreement with Toshiba. [redacted] 25X1

[redacted] Siemens officials believe progress on Megaproject is being delayed by Toshiba's reluctance to share detailed technical information on its one-megabit processing and its heavyhanded attempt to replace Siemens' US suppliers with Japanese firms. In addition, Philips is diluting its effort by conducting a similar research program of its own. Megaproject's present difficulties with one-megabit chips—where the West Europeans already are far behind—threaten to spill over into its research on four-megabit chips. [redacted] 25X1 25X1

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Siemens Seeks To Reduce Dependence on Japan

[redacted]

[redacted] Siemens of West Germany has reinstituted its R&D program for a mainframe computer system. Siemens previously designed and built their own systems, but over the past decade has become increasingly dependent on Fujitsu for mainframe computers. Currently, Siemens does little or no basic R&D in general purpose mainframe technology. This is the first attempt by any of Japan's mainframe partners to reduce their technological dependence. We do not believe, however, that Siemens will be able to produce a system that will have a significant impact on US market share in Western Europe. Siemens's mainframe-technology gap vis-a-vis US and Japanese competitors may be too large to close regardless of the financial commitment from Siemens. Siemens's effort may also threaten its existing mainframe revenues because Fujitsu may consider ending or revising the relationship. [redacted] 25X1 25X1 25X1

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[redacted]

[redacted]

25X1

National Developments

Developed Countries

[redacted]

25X1

Dutch Unions Propose Reduced Workweek

[redacted]

The Dutch socialist trade union federation, FNV, recently announced its intention to press employers for a 36-hour workweek as part of a drive to reduce the 13.1-percent unemployment rate. The federation proposes that the two-hour cut in weekly hours be implemented over a four-year period for large- and medium-sized firms; small firms, however, would be given a longer phase-in period. While a shorter week might preserve present jobs, it probably would have little impact on the unemployment rate. A study by a Dutch union claims employers would probably force workers to increase their production rather than hire more employees. Reduced working hours are not likely to be adopted soon. The government last year abandoned its efforts to shorten the workweek. The main Dutch employers' organization argues the plan will add to labor costs but do little to create new jobs. Pressure on the employers will increase next spring, however, if, as expected, the Labor Party comes to power in the May 1986 elections. [redacted]

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Less Developed Countries

Possible Haitian Petroleum Cutoff

Haiti's failure to pay some $15 million in arrears to its petroleum suppliers may lead to curtailed shipments in coming weeks. US Embassy sources report that extrabudgetary expenditures by the Duvalier regime are blocking negotiations with the IMF and depleting Haiti's foreign exchange reserves. The US Embassy says that public discontent over economic problems is growing. The fragile economy would quickly feel a reduction in oil shipments. Electric power shortages would disrupt communications, transportation, and production at a variety of assembly plants—adding to the unemployment problem. Without a workable program with the IMF, Duvalier probably will look to Washington to strengthen the economy and forestall outbreaks of violence. 25X1 25X1

Trinidad and Tobago Streamlining Sugar Enterprise

The Trinidadian Government's recent plan to trim operations of its sugar producer, CARONI, reflects belated efforts to ease the growing burden of extensive state ownership. The government controls about 80 percent of the economy through 64 jointly or wholly owned companies, only seven of which were profitable in 1984. Although the government fears substantial job losses, the sharp decline in oil revenues has made it increasingly difficult to subsidize these inefficient corporations. CARONI—the largest employer among the state enterprises—received government subsidies of more than $120 million in 1984 alone. According to press reports, the reorganization plan includes the elimination of 4,500 jobs over three years. The CARONI plan probably will enable the opposition National Alliance for Reconstruction, which already enjoys a substantial lead over the ruling People's National Movement in opinion polls, to further capitalize on growing labor concerns that sizable layoffs may be in the offing in other public enterprises. 25X1 25X1

Tunisian Crackdown on Labor

The Tunisian Government is moving against dissident union officials to force them to accept the Prime Minister's wage and austerity measures and to forestall opposition activity. Security forces have arrested more than 400 officials and occupied trade union offices. Senior union leaders are calling for nationwide strikes. The press reports that authorities also discovered and confiscated weapons and copies of Libyan leader Qadhafi's *Green Book*. Wage negotiations have dragged on for months; the government had already closed the union newspaper and stopped the withholding of union dues. Union boss Habib Achour is a longtime opponent of government policies and recently refused to support Tunis's firm stand against Libyan threats. Labor unrest will play into the hands of the Libyans in their efforts to mount subversive operations including possible attacks against US facilities and personnel. 25X1

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Jordan Waiting for Saudi Aid

The US Embassy reports that Jordan has not made any oil payments to Saudi Arabia since midsummer in anticipation that Riyadh will come through with a grant for the oil. The overdue bill will climb to $88 million by mid-November, excluding interest charges on the arrears. Riyadh recently honored its Baghdad pledge to Jordan worth $119 million, but its current budget squeeze may reduce the chances that it will forgive entirely Jordan's oil debt. The overdue oil bill adds to the uncertainties surrounding Jordan's foreign exchange situation. Amman's official foreign exchange reserves began to climb in early summer because of Omani aid and a successful loan syndication, but they fell sharply in August to $435 million—equal to a little more than two month's imports.

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Nigerian Pay Cuts

President Babangida has announced pay cuts for the armed forces, police, and civil service in what may be a crucial test for the new regime. The US Embassy reports that the military pay cuts begun 1 November are on a sliding scale, from 2 percent for the lowest ranks to 20 percent for members of the Armed Forces Military Council, including the President. The government also announced that salaries of all civil servants, as well as those of the staffs of universities and semiofficial organizations, will be cut by up to 15 percent. Civilians will probably applaud the military's pay cuts as a sign of its willingness to share the country's hard times, but they will resent cuts in their own salaries, which have been frozen for nearly two years. By extending austerity to the armed forces, Babangida risks encouraging coup plotting among junior officers—already chronic—and losing essential military support.

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Burma Announces Surprise Currency Recall

Rangoon this week recalled 100, 50, and 20 kyat notes—the first such action since 1964—probably in an attempt to curb illegal economic activities. Old notes will be redeemable from 11 November through the end of the year and apparently will be exchanged one for one up to the income tax threshhold only—hurting blackmarketeers, speculators, and drug dealers who have amassed large sums of illegal cash. The US Embassy reports that the government's action is severely disrupting legal commercial dealings, however, because vendors are no longer accepting the old notes or are discounting them. Moreover, the long-term impact on the black market probably will be limited because Rangoon is unlikely to take steps to liberalize the economy and reduce incentives for these activities.

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Communist

Soviet-East German Trade, 1986-90

The USSR and East Germany last week signed a protocol calling for some increase in East German deliveries in 1986-90 but flat Soviet oil shipments, implying growth of overall trade will be much slower than in recent years. The agreement coordinating economic plans calls for a 28-percent growth in trade

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compared to the previous five-year period, according to the East German news agency, indicating trade will grow about 3 percent annually over the projected 1985 level. East German exports of consumer goods are to rise 40 percent; chemicals, 50 percent. Moscow promised to supply 17.1 million metric tons of oil yearly, the same as in 1985, and slightly higher quantities of natural gas, coal, and iron ore. The indicated growth rate is a sharp reduction from the double-digit rates of recent years, reflecting in part the leveling off of Soviet natural resource deliveries and a slowdown in price increases. The higher level of East German shipments of consumer goods and high-technology items stems from Moscow's demands that its allies support domestic Soviet economic priorities. The announcements by both sides leave key questions unanswered about trade balance, the growth of total East German exports, and the level of East German investments in Soviet natural resource projects. [redacted] 25X1

USSR Steps Up Commercial Space Efforts

[redacted]

The Soviet Union recently publicized Maincosmos, its new space organization for promoting international space efforts. Maincosmos plans to offer satellite launch services in competition with the West European Ariane and the US space shuttle, [redacted] Soviet press reports indicate the organization will also examine proposals for space exploration, research on space technology and equipment, and dissemination of space information. The USSR has launched satellites for Bloc countries, India, and France under the Intercosmos program. In 1984, Moscow offered launch services to the International Maritime Organization for its next-generation navigation satellites, but the bid was rejected. [redacted] 25X1 25X1 25X1

East European Harvest Prospects Worsen

[redacted]

A prolonged drought following a harsh winter has seriously damaged crops in Bulgaria and Romania and to a lesser degree in Yugoslavia, dimming hard currency trade prospects and spelling more belt-tightening for consumers. [redacted] Embassy reporting suggest Bulgarian grain output this year probably will be no more than 7 million tons, more than 20 percent below last year and the worst showing since 1974. A Romanian grain crop of around 16.6 million tons is expected, the smallest crop since 1975. Yugoslavia's grain harvest will probably fare better at 16.2 million tons, near its average. Nonetheless, Belgrade has reported that all crops have suffered this year and expects total agricultural output to fall some 11 percent below last year's production. Agriculture's poor performance will further depress economic growth in these countries—already beset with shortfalls in energy and industry. Supplies of most staples in Yugoslavia, and to a lesser extent in Bulgaria, should be adequate, but spot shortages and higher prices are likely to lead to increased consumer grumbling. In Romania an already poor food supply will get worse. [redacted] 25X1 25X1 25X1

China's 1985 Grain Production Falls

[redacted]

China's grain output will drop 5 to 10 percent this year from the 1984 record of 407 million metric tons because of bad weather and reduced production incentives. Stockpiles will make up the shortfall, however, and a significant increase in grain imports is unlikely. The net grain reduction will slow China's

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ambitious plans to export grain and to expand the livestock industry. Beijing, concerned that declining grain production will hinder Chinese modernization plans, is adjusting its rural policies to assure that next year's grain output will increase. This year, peasants shifted too much of their labor and resources from grain production to more profitable crops and rural industry. Press reports indicate that policymakers will raise grain procurement prices next year to encourage grain production, stabilize the rural economic sector, and mollify party conservatives who are using falling grain figures to criticize reform. [redacted] 25X1

Chinese Funding for Basic Research

[redacted]

China is establishing "national science foundations," modeled on the US National Science Foundation, to sponsor basic research in selected areas. A Geological Sciences Foundation is already operating, while a much larger National Natural Science Foundation (NNSF) reportedly will be established in January 1986. Between $35-40 million will be allocated to the NNSF; the geological foundation budget will be $1.7 million in 1986. The science foundations, part of the S&T reforms Beijing announced last March, are intended to improve the quality of basic research in China through peer review and competitive funding [redacted] 25X1 25X1

Hanoi Seeking Humanitarian Aid

[redacted]

Because foreign exchange reserves are insufficient to pay for large-scale rice imports, Hanoi is appealing for international aid following a series of typhoons since August that killed over 800 people and extensively damaged rice fields. Vietnamese officials claim over 1 million metric tons of paddy have been damaged or destroyed, compared to less than 800,000 tons last year. The Ministry of Agriculture is projecting 1985 foodgrain output at 17.3 million tons or less, down from 17.9 million tons in 1984. Vietnam had achieved near self-sufficiency in rice in 1983 after boosting output at a 6-percent average annual rate from 1976 to 1983. [redacted] 1985 rice import requirements at 500,000 tons—more than 50 percent above 1984 levels. [redacted] 25X1 25X1 25X1